Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Application by BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana	)	CC Docket No. 97-231

AFFIDAVIT OF
PATRICIA A. MCFARLAND
ON BEHALF OF AT&T CORP.

Patricia A. McFarland, being first duly sworn upon oath, does hereby depose and state as follows:

I. AFFIANT

1. My name is Patricia A. McFarland. My business address is 1200 Peachtree Street N.E., Room 5070, Atlanta, Georgia 30309.

2. I am employed by AT&T Corp. ("AT&T") as a manager in the Regulatory Chief Financial Officer ("RCFO") organization. As such, I am responsible for AT&T regulatory financial activities in a number of states and for a number of subject matter areas, such as local exchange carrier ("LEC") cost analysis functions. I have testified with regard to the retail costs incumbent LECs will avoid in the provision of wholesale local service on behalf of AT&T in recent arbitration and resale proceedings in Louisiana, Tennessee, Alabama and Kentucky.

3. I have a degree in Business Administration with a concentration in Accounting from Oglethorpe University in Atlanta, Georgia.

4. In 1968, I began my career at Pacific Telephone Company in San Francisco where I held a variety of Operator Services staff and line positions. I primarily performed payroll, budgeting and scheduling functions. In 1982, at divestiture, I transferred to AT&T and assumed responsibility for LEC billing in conjunction with California Operator Services Shared Network Facilities Agreements. In 1985, I accepted the position of Assistant Manager - Accounting Regulatory Support responsible for AT&T financial regulatory matters for Oregon and Washington. In May of 1991, I transferred to my present organization in Atlanta, Georgia. Initially, I was responsible for AT&T financial regulatory matters for the south central states. In 1995, I accepted my current position of Manager - RCFO.

II. SCOPE OF AFFIDAVIT AND SUMMARY

5. Section 272 of the Communications Act of 1934, as amended by the Federal Telecommunications Act of 1996 ("Act"), bars a Bell Operating Company ("BOC") from providing in-region interLATA service unless it provides such service through an affiliate that meets the separation and nondiscrimination requirements of that section. By imposing a variety of accounting and nonaccounting safeguards, section 272 attempts both to prevent a BOC from discriminating against its competitors and in favor of its long-distance

affiliate, and to prevent a BOC from subsidizing its affiliate by recovering the affiliate's costs through the BOC's local and exchange access service customers.[1]

6. In its recent Ameritech Michigan Order,[2] the Commission confirmed that the obligations and restrictions under section 272 were of "crucial importance," id. at ¶ 346, and that the BOCs and their section 272 affiliates have been required to comply with those obligations and restrictions since the date the Act was passed, February 8, 1996. Id. at ¶ 371. The Commission also confirmed that to satisfy the public disclosure requirements of section 272(b)(5), a BOC must disclose detailed information regarding the terms and conditions of each transaction between the BOC and its section 272 affiliate, including the rates for each transaction. Id. at ¶ 369.

7. The purpose of this Affidavit is to discuss the failure of BellSouth Telecommunications, Inc. ("BellSouth") and its section 272 affiliate, BellSouth Long

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[1] "Congress ... enacted section 272 to respond to the concerns about anticompetitive discrimination and cost-shifting that arise when the BOC enters the interLATA services market in an in-region state in which the local exchange market is not yet fully competitive." Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Action of 1934, As Amended, CC Docket No. 96-149, Second Order on Reconsideration, FCC 97-222 (released June 24, 1997), ¶ 5. The section 272 affiliate is required, among other things, to operate independently from the BOC, to maintain separate books and records, to have separate officers, directors, and employees, and to conduct all transactions with the BOC on an arm's length basis, reducing such transactions to writing, available for public inspection. § 272 (b). In addition, the BOC is prohibited from discriminating in favor of its section 272 affiliate in the provision of "goods, services, facilities, and information, or in the establishment of standards." § 272(c).

[2] Application of Ameritech Michigan Pursuant To Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services in Michigan, CC Docket No. 97-137, Memorandum Opinion and Order (released Aug. 19, 1997) ("Ameritech Michigan Order").

Distance, Inc. ("BSLD"),[3] to meet their burden of establishing that they will operate in compliance with section 272 if and when BellSouth is granted authorization to provide in-region interLATA services. In its application, BellSouth has not provided the sort of detailed, specific evidence concerning its past and current transactions with BSLD that is necessary to permit the Commission to come to any conclusion as to whether it will comply with section 272. Indeed, the evidence presented by BellSouth plainly demonstrates that if it were granted interLATA authority today, it would not be in compliance with section 272.

8. Although BellSouth has stated that it already provides fifteen different categories of services to BSLD having a total cost of nearly $9.2 million, it has refused to publicly disclose critical details regarding most of these transactions, as required by section 272(b)(5) and the Commission's Accounting Safeguards Order.[4] Indeed, in defiance of the Commission's Ameritech Michigan Order, BellSouth has taken the position in its current application that "[BellSouth] and BSLD need not conduct or report transactions in accordance with the requirements of section 272 prior to receiving interLATA authorization." Brief in Support of Application by BellSouth for Provision of In-Region InterLATA Services in Louisiana ("BellSouth Br.") at 76. Furthermore, BellSouth has directly defied the

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[3] According to BellSouth, BSLD is a wholly-owned subsidiary of BellSouth Long Distance Holdings, Inc. which in turn is a wholly owned subsidiary of BellSouth Corporation. Affidavit of Victor E. Jarvis, in the Matter of Application by BellSouth Corporation for Provision of In-Region, InterLATA Services in Louisiana ("Jarvis Aff.") at 2.

[4] Implementation of the Telecommunications Act of 1996, Accounting Safeguards Under the Telecommunications Act of 1996, CC Docket No. 96-150, Report and Order (released Dec. 24, 1996) ("Accounting Safeguards Order"), ¶ 122.

Commission by failing to post "a detailed written description . . . on the Internet within 10 days" of all transactions between BellSouth and BSLD, nor has it made detailed information regarding all transaction between BellSouth and BSLD "available for public inspection at the principal place of business of [BellSouth]." Accounting Safeguards Order, ¶ 122.

9. In addition, the vague, limited descriptions of many of the services provided to BSLD by BellSouth make it impossible to determine whether BellSouth has complied with the Commission's accounting rules or otherwise has met the antidiscrimination requirements of section 272. Most of these descriptions provide no rates or prices for the services and provide no details regarding other basic terms and conditions. Furthermore, in the few instances where BellSouth has provided enough information to evaluate these services, there is stark evidence that BellSouth has been and will be providing preferential treatment to BSLD in violation of section 272.

10. BellSouth also has not identified any internal systems or procedures that it has instituted specifically to address the requirements of section 272 and to attempt to protect against violations of section 272. I am familiar with such internal compliance systems instituted by other BOCs -- such as oversight committees to review section 272 transactions, and customer contact points to protect against "off-the-record" transactions -- and I believe that such compliance programs are essential for a BOC to establish that it is ready and able to comply with section 272.

11. Nor has BellSouth provided any information or evidence to explain how it will identify, end, and correct, through a "true-up" or otherwise, any improper cross-subsidization and discrimination that may already have occurred. The risk that such

inappropriate subsidization or discrimination has occurred is substantial, because BellSouth apparently has been operating under the view that none of the transactions between it and BSLD have been subject to the restrictions of section 272. Unless some attempt is made to identify and rectify any such impermissible transactions, BSLD will be able to enter the interLATA market with improper subsidies or other illicit and anticompetitive advantages.[5]

12. Finally, BellSouth has asserted, again in defiance of the Commission's Order, that it will instruct its customer service representatives to recommend BSLD long distance service to customers calling to order local exchange service, and not to recite a list of long distance carriers unless the customer affirmatively requests such information.[6] This proposed marketing practice is virtually identical to the telemarketing script that the Commission found unacceptable in its Ameritech Michigan Order. Ameritech Michigan Order, ¶¶ 375-76.

13. Ultimately, BellSouth's evidence that it will comply with section 272 is simply paper promises. These assurances are not due any significant weight, especially in light of the fact that in the past auditors have found BellSouth's behavior to be

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[5] See Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, CC Docket No. 96-149, FCC 96-489 (released Dec. 24, 1996) ("Non-Accounting Safeguards Order"), ¶¶ 9-13.

[6] Affidavit of Alphonso J. Varner, in the Matter of Application by BellSouth Corporation for Provision of In-Region, InterLATA Services in Louisiana ("Varner Aff."), ¶ 223.

"obstructionist," preventing the auditors from even being able to form an opinion regarding whether BellSouth was improperly subsidizing affiliates.[7]

III. BELLSOUTH MUST PRESENT SPECIFIC, TANGIBLE EVIDENCE, NOT MERE PROMISES, TO MEET ITS BURDEN UNDER SECTION 271(d)(3).

14. In the Ameritech Michigan Order, the Commission again made clear that BOCs bear the burden under section 271(d)(3) of establishing that they will operate in compliance with section 272 if granted interLATA authority. Ameritech Michigan Order, ¶¶ 43, 371. "Paper promises do not, and cannot, satisfy a BOC's burden of proof." Id. at ¶ 55. The requirement that a BOC come forward with specific, tangible evidence is especially appropriate in the context of section 272 compliance, because most of the evidence relevant to such a determination lies exclusively in the hands of the BOCs and their affiliates.

15. For these reasons, simple pledges by BellSouth that it "has been" or that it "will be" in compliance with section 272 should be given no weight. Rather, BellSouth must be called upon to come forward with specific, concrete evidence that shows, among other things:

- that all BellSouth/BSLD transactions, whether involving assets, information, or services, and including "chain transactions" involving a separate nonregulated affiliate,[8] have been reduced to writing and made available for public inspection;

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[7] See infra ¶¶ 40-42.

[8] The Commission repeatedly has made clear that the affiliate transaction rules govern "chain transactions" where an unregulated affiliate stands between the BOC and the section 272 in the provision of assets, information, or services. See Accounting Safeguards Order, ¶¶ 183, 251; Non-Accounting Safeguards Order, ¶ 309; Ameritech Michigan Order, ¶ 373.

- that all BellSouth/BSLD transactions (again including "chain transactions") to date have been conducted on an "arm's length" basis and have been nondiscriminatory;

- that detailed internal accounting and tracking systems are in place and operational so as to comply with the Accounting and Non-Accounting Safeguards Orders and with section 272;

- that internal oversight procedures are in place to ensure that all affiliate transactions are conducted on an "arm's length" basis and are non-discriminatory;

- that asset allocations required by the Accounting Safeguards Order have been fairly established;

- that methods of valuing transactions between BellSouth and BSLD meet Commission guidelines (such as the derivation of the "fully distributed costs" that BellSouth repeatedly references in its general descriptions of services provided to BSLD) and have been fairly and accurately established;

- that the transactions between BellSouth and BSLD have not, and do not, provide impermissible cross-subsidization of BSLD; and

- that, as discriminatory conduct and cross-subsidization may already have occurred, BellSouth and BSLD have procedures in place to "true-up" these past transactions so that BSLD does not enter the interLATA market with unlawful pre-authorization subsidies or other unlawful advantages from BellSouth.

16. The evidence that BellSouth must be required to present should include, among other things, the following, all of which are readily available to BellSouth:

- financial reports of BellSouth and BSLD;

- specific terms and conditions of asset transfers and other transactions between BellSouth and BSLD, including transfers, sales and/or leases of property, equipment, and information, and employee transfers;

- the specific terms and conditions of service transactions conducted between BellSouth and BSLD;

- the precise extent to which the affiliate has used the services of BellSouth employees in the planning, construction, or maintenance of BSLD's network and how such services were accounted for; and

- the specific nature and extent of funding of BSLD.

17. The absence of these types of specific evidence, without any justifying explanation, should raise immediate doubts as to whether a BOC and its section 272 affiliate have in fact operated in compliance with section 272. A BOC cannot hope to meet its burden under section 271(d)(3) without such a presentation.

18. As I discuss more fully below, BellSouth's application fails to present the type of detailed, concrete evidence necessary to make any meaningful evaluation of its assertions that it will comply with section 272. Indeed, BellSouth repeatedly states its disagreement with the Commission regarding its obligations under section 272, stating that it is under no current obligation to ensure that its transactions with BSLD are publicly disclosed, are arm's length in nature, or otherwise comply with section 272 prior to being granted interLATA authority.[9] In addition, BellSouth also states that it intends to follow the same marketing practices found unacceptable in the Ameritech Michigan Order.

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[9] Even BellSouth concedes, however, that current compliance is "highly relevant" as evidence of future compliance if the BOC claims that it is currently in compliance. BellSouth Br. at 76. Therefore, even under BellSouth's own argument, its failure to reduce all transactions between BellSouth and BSLD to writing and post these transactions for public inspection is "highly relevant," because BellSouth does, in fact, claim that it complies with section 272. See Affidavit of Guy L. Cochran, in the Matter of Application by BellSouth Corporation for Provision of In-Region, InterLATA Services in Louisiana ("Cochran Aff."), ¶¶ 9-13, 21; Varner Aff., ¶¶ 196, 203, 205, 207, 210-11, 213, 215. In any event, the fact that BellSouth seeks reconsideration of the Ameritech Michigan Order does not exempt it from complying with the Commission's orders during the pendency of its petition. See 47 U.S.C. § 405.

IV. BELLSOUTH CURRENTLY IS NOT IN COMPLIANCE WITH THE DISCLOSURE REQUIREMENTS OF SECTION 272(b)(5).

A. The Written Descriptions Of The Types Of Services Provided By BellSouth To BSLD Do Not Satisfy The Requirement That Each Transaction Be "Reduced To Writing."

19. Section 272(b)(5) requires that each transaction between BellSouth and its section 272 affiliate BSLD be "reduced to writing and available for public inspection." In the Accounting Safeguards Order, the Commission determined that this "reduced to writing" requirement meant "that the description of the asset or service and the terms and conditions of the transaction should be sufficiently detailed to allow us to evaluate compliance with our accounting rules." Accounting Safeguards Order, ¶ 122. In the Ameritech Michigan Order, the Commission made clear that such descriptions must "disclose the actual rates for [the BOC's] transactions with its section 272 affiliate." Ameritech Michigan Order, ¶ 369.

20. These public disclosure requirements are critical to enabling CLECs, IXCs, and the Commission to assess, among other things, (i) whether the BOC is impermissibly subsidizing the section 272 affiliate, and (ii) whether the BOC is impermissibly engaging in transactions with its section 272 affiliate with terms, conditions, or arrangements that are more favorable than those offered to CLECs or to IXCs. Furthermore, the information disclosed must be "detailed" and sufficient "to allow [the Commission] to evaluate compliance with [its] accounting rules." Accounting Safeguards Order, ¶ 122. Obviously, a simple disclosure that certain types of transactions occurred and the general subject matter of those transactions is insufficient. See Ameritech Michigan Order, ¶ 367.

21. The meager information BellSouth has disclosed concerning its transactions with BSLD clearly does not comply with section 272(b)(5) and the Accounting Safeguards Order. The only information concerning past and ongoing transactions between BellSouth and BSLD presented in this section 271 application is contained in the affidavit of Victor E. Jarvis. That affidavit does not provide descriptions of individual transactions, but rather broadly identifies 15 categories of services that BellSouth has provided to BSLD, such as "Customer Billing Services," "Project Management," "Collocation," and "Mail Service." Jarvis Aff. at 6-11. Not one of the descriptions provided under these service category headings includes prices, rates, or other terms and conditions for any particular transaction. Instead, each description of a service category provides only a total cost figure for all the transactions grouped under that category.[10] For example, the "Information Technology - Billing Systems" category states that BellSouth has provided BSLD "services associated with the development, design, coding, and testing of systems," and "the amount for these services totaled $2,995,400." Jarvis Aff. at 8-9. BellSouth does not provide specific descriptions of the goods and services rendered and other than seven contracts available on its internet site and its corporate headquarters, it does not provide any contract terms. Moreover, BellSouth did not produce a certified statement from an officer of BellSouth concerning these transactions, as required by the Accounting Safeguards Order. See Accounting Safeguards Order, ¶ 122.

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[10] According to BellSouth, the costs of these fifteen categories of services for BSLD totals nearly $9.2 million. Jarvis Aff. at 7-11.

22. Furthermore, although BellSouth states that its application includes a "description of all transactions between [BellSouth] and BSLD to date," BellSouth Br. at 76 (emphasis added), the Jarvis affidavit does not, in fact, disclose all the transactions to date between BellSouth and BSLD. Indeed, the Jarvis affidavit states that the service descriptions are limited to services provided "through August 31, 1997." Jarvis Aff. at 7. BellSouth's failure to provide descriptions of all transactions occurring after August 31, 1997, is a direct violation of the Commission's Ameritech Michigan Order. See Ameritech Michigan Order, ¶ 370. BellSouth has given no explanation for this apparently arbitrary cut-off date.[11]

23. BellSouth's application does not provide specific descriptions of the goods and services rendered to BSLD. Nor does the application's description of past transactions include specific contract terms and conditions.[12] The vague descriptions that are provided raise a host of important questions that must be answered before the transactions can be judged under the requirements of section 272. For example, BellSouth states that it has provided "miscellaneous administrative services" for BSLD, Jarvis Aff. at 6, but does not specifically identify these services. Similarly, BellSouth states that it provided "initial planning services" for BSLD, Jarvis Aff. at 8, without identifying those "planning services."

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[11] This is the second time that BellSouth has submitted a brief to the Commission that falsely states that it has disclosed all transactions "to date," BellSouth Br. at 76, when it has chosen to deliberately cut-off disclosure over two months before the filing date of its 271 application.

[12] BellSouth's internet site includes seven contracts between BellSouth and BSLD. These same seven contracts also are available at BellSouth's corporate headquarters. BellSouth, however, has not submitted these contracts as part of its section 271 application. In any event, the disclosure of these contracts is on its face inadequate, because BellSouth has identified no fewer than 15 separate types of services that it has provided to BSLD.

24. BellSouth does not discuss whether written agreements have been entered into between BellSouth and BSLD for all these services. If written agreements exist, they must be disclosed by BellSouth before any judgment can be made as to the arm's length character of these transactions. If written agreements do not exist for all these services, the lack of written agreements is itself a violation of section 272.[13] § 272(b)(5).

25. BellSouth's repeated assertion that it provides services to BSLD at "fully distributed costs" is also inadequate to meet its burden of showing compliance with the applicable accounting rules. At a minimum, BellSouth must demonstrate what these "fully distributed costs" actually were and must include both rates and the terms and conditions for the services that BellSouth provided to BSLD. "[A] statement of the valuation method used, without the details of the actual rate" does not meet BellSouth's legal obligation under the Accounting Safeguards Order. Ameritech Michigan Order, ¶ 369 (emphasis added).

B. BellSouth Has Violated The Requirements Of The Statute And The Accounting Safeguards Order By Failing To Make Transactions Between BellSouth and BSLD "Available For Public Inspection."

26. As noted above, section 272(b)(5) requires that "all transactions" between a BOC and its section 272 affiliate not only be "reduced to writing," but also be "available for public inspection." In the Ameritech Michigan Order, the Commission found that these disclosure requirements took effect on passage of the Act on February 8, 1996,

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[13] BellSouth simply is not at liberty to conduct its dealings with BSLD on any basis other than through written agreements, and those agreements must be available for public inspection. Section 272(b)(5) requires that all "transactions" between a BOC and its affiliate must be "reduced to writing," while the Accounting Safeguards Order provides that a "transaction" exists "[o]nce the BOC and its affiliate have agreed upon the terms and conditions." Accounting Safeguards Order, ¶ 124.

and that, since that time, BOCs and their section 272 affiliates have been required to make publicly available all transactions for information, services, or facilities in which they have been engaged. Ameritech Michigan Order, ¶ 371.

27. The Accounting Safeguards Order held that section 272(b)(5)'s public disclosure obligation requires affiliates, "at a minimum, to provide a detailed written description of the asset or service transferred and the terms and conditions of the transaction on the Internet within 10 days of the transaction through the company's home page." Accounting Safeguards Order, ¶ 122. The Accounting Safeguards Order's public disclosure obligations became effective on August 12, 1997. See Accounting Safeguard Rule Changes Requiring OMB Approval Soon to be Effective, Public Notice, DA 97-1669 (released Aug. 5, 1997).

28. BellSouth has been, and continues to be, in violation of disclosure requirements under section 272(b)(5) and the Accounting Safeguards Order. BellSouth claims that "BSLD is publishing all of its executed written agreements with [BellSouth] at [its] internet site." Jarvis Aff. at 11. But although BellSouth concedes that it has engaged in fifteen different transactions with BSLD, id. at 6-11, it has only provided written documentation for four of these transactions.[14] Therefore, if BellSouth's statement that "BSLD [has published] all of its executed written agreements" is true, BellSouth has violated

[14] BellSouth has posted on its Internet site a collocation agreement; a facility use agreement; an AIN agreement and two agreements for end-to-end testing. There are two additional agreements for fraud management and billing and collection services which are not included among the 15 past transactions discussed in the Jarvis affidavit. See generally Jarvis Aff. at 7-10.

section 272(b)(5) by not reducing "all transactions" between BellSouth and BSLD "to writing." On the other hand, if BellSouth's statement is false, it has violated section 272(b)(5) by not making these agreements available for "public inspection." Furthermore, there are six transactions that BellSouth has conceded were ongoing through August, 1997,[15] for which BellSouth has not posted information on the internet in violation of the Accounting Safeguards Order, ¶ 122.

C. Even The Limited Disclosure Made By BellSouth Reveals A Number Of Transactions That Appear On Their Face To Be Discriminatory.

29. Not only has BellSouth provided inadequate disclosure of its transactions with BSLD, but even the limited disclosure that BellSouth has undertaken reveals transactions that on their face appear discriminatory. For example, BellSouth has provided a copy of a collocation agreement between BellSouth and BSLD[16] which is clearly discriminatory on its face. The BSLD Collocation Agreement is for two years from the date BSLD's "equipment becomes operational."[17] BSLD has 180 days to make its equipment operational from the date BellSouth informs it that the space is ready, plus an additional "grace" period of at least 30 days. BSLD Collocation Agreement, II(B). Thus, BSLD can delay the start of its two-year contract period by 210 days. By contrast, when a CLEC signs

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[15] These six transaction are: Customer Billing Services; Project Management; Sales Channel Planning and Design; Investment Related Costs- PCs; Telecommunications Services; and Mail Service. Jarvis Aff. at 7-11.

[16] Collocation Agreement By and Between BellSouth Telecommunications, Inc. and BellSouth Long Distance, Inc. ("BSLD Collocation Agreement") (Attachment 1).

[17] BSLD Collocation Agreement, II(A).

a collocation agreement with BellSouth, it receives collocation space for two years from the date the agreement is signed, regardless of when its equipment becomes operational.[18] Furthermore, BellSouth may delay starting the two-year (plus 270 day) contract period by merely not "releas[ing] the collocation space for occupancy" to BSLD. BSLD Collocation Agreement, V(B). Until BellSouth releases this space, BSLD neither pays any monthly charges for the collocation space, nor does its two year agreement begin to run. Id. at II(A and B), V(B). Therefore, BSLD pays less for its collocation space than do the CLECs because the fixed costs of the agreement are spread out over a longer period than the two year agreements that the CLECs must sign. In addition, BellSouth may illegally subsidize BSLD after BellSouth receives interLATA authority by merely not "starting the clock" on BSLD's contract, allowing BSLD to reserve collocation space without having to pay any monthly fees. The fact that BellSouth chose to provide different terms to BSLD than the CLECs demonstrates that BellSouth does not treat BSLD impartially.

30. BellSouth also appears to provide preferential service to BSLD for billing and collection services. BellSouth vaguely states that billing and collection services provided to BSLD will be "much like" those provided to IXCs. Cochran Aff. ¶ 26(i). Section 272, however, requires BellSouth to make the same billing and collection services available to other IXCs. § 272(c)(1) and (e)(2). Moreover, section 272 requires that BellSouth not offer such billing and collection services on terms that would only be acceptable to its affiliate (even though equally "available" to all IXCs), such as requiring a

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[18] BellSouth Physical Collocation Master Agreement ("CLEC Collocation Agreement") (Attachment 2), (I)(A) and II(A).

carrier to commit a large percentage of its growth to the BOC. See Non-Accounting Safeguards Order, ¶ 212.

31. These examples of discriminatory transactions between BellSouth and BSLD based on the limited disclosure provided so far highlight the need to have complete disclosure of the terms and conditions of all their prior transactions. Based on the disclosure that has been made to date, there simply is no basis to conclude that BellSouth and BSLD will comply with section 272 if granted interLATA authority.

32. BellSouth has deliberately defied the Commission by failing to post all applicable transactions on the Internet. Accounting Safeguards Order, ¶ 122. In addition, BellSouth has defied the Commission by failing to describe all the transactions between BellSouth and BSLD with "sufficient[] detail to allow [the Commission] to evaluate compliance." Id. Furthermore, BellSouth has provided illegal subsidies to BSLD which could continue even after the Commission grants BellSouth InterLATA authority. Consequently, BellSouth has not come close to meeting its obligations under section 272 and the Accounting Safeguards Order.

V. BELLSOUTH HAS NOT PRESENTED ANY TANGIBLE EVIDENCE THAT IT HAS PROCEDURES OR SYSTEMS IN PLACE TO PROTECT AGAINST VIOLATIONS OF SECTION 272.

33. The Telecommunications Act has required BellSouth to change the way it does business. Section 272 itself presents a series of obligations that BellSouth must face, such as requiring it to create a wholly separate company to provide a telecommunications service that must operate independently of BellSouth, and that must not be provided services,

information, or facilities on terms any more favorable than those provided to the competitors of BellSouth.

34. In the face of these types of significant changes in the way business must be done, basic accounting principles require that BellSouth create new internal systems and procedures to protect against violations of its new legal obligations. In particular, when organizations are undergoing major change, one of the most important internal controls is risk assessment.[19] Although BellSouth promises compliance and coverage for BellSouth employees, it provides no support or documentation describing procedures that BellSouth has implemented in response to the changing risks due to BellSouth's 271 application. BellSouth's business-as-usual attitude relies on its established control environment to provide internal discipline and structure. Because BellSouth has shown in its previous dealings with affiliates its ability to obstruct audits and benefit from delays inherent in the regulatory process, the Commission should be especially vigilant in regards to internal control.

35. For example, BellSouth's affidavits refer generally to internal audits that have been conducted (without identifying the specific purposes of these audits, the procedures followed, or their results), and appear to suggest that these internal audits will continue and will protect against violations of section 272. Cochran Aff., ¶ 24; Jarvis Aff. at 4. But for such internal audits to be effective in identifying violations of section 272, auditing procedures must be revised to include methods specifically designed to seek out and

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[19] "[R]isk assessment for financial reporting purposes is its identification, analysis, and management of risks relevant to the preparation of financial statements that are fairly presented in conformity with generally accepted accounting principles." AICPA Professional Standards, Statements on Auditing Standards, Vol. I., AU 319.28.

evaluate transactions for assets, services and information that were not recorded or subject to a written agreement. No reliable or accurate evaluation of section 272 compliance can be made without identifying (or confirming the non-existence of) unrecorded transactions, because it is just such unrecorded dealings that provide the most ready means by which BellSouth and BSLD could engage in unfair cross-subsidization or other anticompetitive activities. BellSouth provides no specific evidence to show that its auditing program has been revised to address the unique compliance issues raised by section 272.

36. BellSouth has not identified any internal systems or procedures that it has instituted specifically to address the requirements of section 272 and to attempt to protect against violations of section 272. BellSouth only promises that it "will develop a process to ensure compliance with Section 272" at some unspecified point in the future.[20] Indeed, BellSouth acknowledges that it has not even taken the preliminary step of conducting employee training on section 272 obligations,[21] despite the fact that its employees are actively engaged in providing substantial services and information to BSLD. See Jarvis Aff. at 6-11. Without evidence of such systems or procedures, there is no basis to conclude that BellSouth is ready and able to comply with section 272. These systems and procedures must

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[20] See Affidavit of George F. Agerton, in the Matter of Application by BellSouth Corporation for Provision of In-Region, InterLATA Services in Louisiana, ("Agerton Aff."), ¶ 2.

[21] Agerton Aff., ¶ 11. BellSouth presents some information on employee training it has conducted concerning its obligations under sections 251 and 252 of the Act. Id. at ¶¶ 6-10. The obligations under section 272, however, substantially differ from those arising under sections 251 and 252.

address the following compliance problems, among others, raised in the context of section 272:

(i) BSLD's workforce includes a significant number of employees who formerly worked at BellSouth (although BellSouth is silent on the precise number of former BellSouth employees now at BSLD). These BSLD employees will have both the incentive and the ability to seek and obtain favorable treatment from their former coworkers at BellSouth, which obviously would be impermissible under section 272.

(ii) BSLD and BellSouth employees will have an incentive to engage in "off-the-record" transactions, especially concerning proprietary information such as CPNI. Such "off-the-record" transactions will be especially difficult to identify and evaluate through any internal or external audit.

(iii) BSLD employees formerly employed by BellSouth have an incentive to take with them, and use, BellSouth proprietary information without accounting for this acquisition of information and without offering this information to competitors.

(iv) BSLD and BellSouth will have a strong incentive to share employee services on an ad hoc basis without properly accounting for such services.

37. The type of compliance programs instituted by other BOCs with which I am familiar include procedures requiring that all transactions between a BOC and its section 272 affiliate be reviewed by an oversight committee to confirm its compliance with section 272. In this way the BOC can separate the process of evaluating section 272

compliance from the employees who are most interested in seeing the transaction completed. In addition, at least one BOC has stated its intent to require that all transactions proceed through specified customer contact points, which can help to ensure that affiliates, CLECs, and IXCs each receive the same access to BOC facilities, information, and services, and which protects against ad hoc "off-the-record" transactions.

38. I view compliance programs such as these, which are specifically geared to the unique obligations posed by section 272, as a prerequisite for a BOC to establish that it is ready and able to comply with section 272. BellSouth's failure to present any tangible evidence of its implementation of such programs, despite having engaged in substantial ongoing transactions with BSLD, shows that it is not prepared to provide interLATA service in compliance with section 272.

VI. BELLSOUTH'S PROPOSED TELEMARKETING FOR INBOUND CALLS IS VIRTUALLY IDENTICAL TO THE TELEMARKETING SCRIPT REJECTED IN THE AMERITECH MICHIGAN ORDER.

39. BellSouth states that, once it begins offering BSLD long-distance service under a joint marketing agreement, it will instruct its customer contact representatives to "advise the customer that a number of companies provide long distance, recommend BSLD and offer to read from a list of available carriers." Varner Aff., ¶ 223. BellSouth has identified the following language as acceptable for its customer service representatives who receive inbound calls from customers requesting new service or a change in existing service:

> "You have many companies to choose from to provide your long distance service. I can read from a list the companies

> available for selection, however, I'd like to recommend BellSouth Long Distance." Id.

BellSouth has stated, further, that its customer service representatives will read a list of available long distance carriers only "if the customer requests that the list be read." Id. at ¶ 224.

40. In the Ameritech Michigan Order, the Commission held that the following suggested inbound telemarketing script "would violate the 'equal access' requirements of section 251(g):

> "You have a choice of companies, including Ameritech Long Distance, for long distance service. Would you like me to read from a list of other available long distance companies or do you know which company you would like."

Ameritech Michigan Order, ¶¶ 375-76.

41. The anticipated telemarketing by BellSouth[22] thus is virtually identical to the script the Commission rejected in the Ameritech Michigan Order as "inconsistent on its face with our requirement that a BOC must provide the names of interexchange carriers in random order." Ameritech Michigan Order, ¶ 376. Indeed, to the extent the BellSouth script differs from the Ameritech script, it is even more objectionable, because it actively promotes BSLD service, while the Ameritech script simply identified the availability of Ameritech long distance service.

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[22] BellSouth contends that it "does not use verbatim scripts for such customer contacts." Varner Aff., ¶ 223. But without verbatim scripts, the Commission will not be able to ascertain whether BellSouth agents will comply with the equal access requirement. Furthermore, BellSouth does not offer any evidence that it has established any internal procedures to monitor its agents' discussions with customers to ensure that equal access is enforced and that problems are expeditiously rectified.

42. As the Commission concluded in the Ameritech Michigan Order, section 251(g) of the Act specifically continues in effect the equal access requirements, thus mandating that the required equal access disclosures be made on all inbound calls prior to any marketing of the affiliate's long distance service. See Ameritech Michigan Order, ¶ 376. Moreover, if customers express a preference for a particular IXC other than the affiliate, either before or after the equal access disclosures are made, then the BOC representative may not market the affiliate's services or otherwise attempt to cause such customers to change their mind.

43. BellSouth has not even attempted to distinguish its proposed telemarketing practices from the practices the Commission rejected in the Ameritech Michigan Order, and instead simply argues that the Commission's Ameritech Michigan Order was wrong in this respect. BellSouth Br. at 79-80. Although BellSouth seeks reconsideration of the Commission's Order on marketing practices, BellSouth is obligated to comply with existing Commission requirements. See 47 U.S.C. § 405.

VII. BELLSOUTH AND BSLD HAVE NOT PRESENTED ANY PLAN TO IDENTIFY AND CORRECT PAST DISCRIMINATION OR SUBSIDIZATION.

44. When a BOC elects to provide in-region interLATA service through a pre-existing affiliate, as BellSouth has done, the BOC must present evidence to detail how it will identify, end, and correct, through a "true-up" or otherwise, all improper cross-subsidization and discrimination that may already have occurred prior to its application. The risk that such inappropriate subsidization or discrimination has occurred is substantial in this case, because BellSouth has admitted engaging in numerous transactions with BSLD and has

stated that it has been operating to date under the view that none of the transactions between it and BSLD have been subject to the restrictions of section 272 or the Accounting Safeguards Order. BellSouth Br. at 76.

45. BellSouth has not presented any evidence that it has established procedures to identify and correct any transactions that are not in compliance with section 272 and the Accounting Safeguards Order.[23] Unless BellSouth is called upon to identify and rectify any such past impermissible subsidies or transactions, BSLD would be able to enter the interLATA market with the very anticompetitive advantages that section 272 was designed to prevent. BellSouth has not even attempted to make such a showing.

VIII. BELLSOUTH'S PAST COMPLIANCE DIFFICULTIES PROVIDE A SUBSTANTIAL BASIS TO DOUBT BELLSOUTH'S PAPER PROMISES TO COMPLY WITH SECTION 272.

46. BellSouth has suggested that any section 272 compliance problems that it experiences will be uncovered and quickly rectified by either internal or external audits. See Cochran Aff., ¶24; Jarvis Aff. at 4. BellSouth's recent compliance history, however, demonstrates that neither internal nor external audits will ensure that BellSouth will comply with section 272, and give substantial reason to doubt BellSouth's current paper promises of future compliance.

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[23] Even under BellSouth's view that it does not need to comply with section 272 until it receives interLATA authority, BellSouth Br. at 76, it currently must have procedures in place to identify and correct transactions that are not in compliance with section 272 and the Accounting Safeguards Order. Because BellSouth has not presented any evidence of such procedures, BellSouth has failed to meet its burden of proving that it will be in compliance with section 272 once it receives interLATA authority.

47. For example, the results of a joint federal and state audit of BellSouth's dealings with its affiliates[24] gives little reason to believe BellSouth's current claims that it will act in compliance with section 272. The Joint Audit, undertaken on behalf of the Commission and the National Association of Regulatory Utility Commissioners, "attempted to evaluate whether cross-subsidy exists between [BellSouth's] regulated and non-regulated operations."[25]

48. The audit team stated that BellSouth made it difficult for them to render an opinion regarding whether BellSouth was subsidizing nonregulated affiliates because of BellSouth's "consistent pattern of obstructionist behavior," which continued for at least eighteen months.[26] Furthermore, the audit team found that due to the lack of cooperation on the part of BellSouth that "many of the audit objectives were not fulfilled."[27] The results of the Joint Audit demonstrate that the Commission should give little weight to BellSouth's paper promises that 272 problems will be identified and quickly rectified by internal and external audits.

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[24] Regional Audit of BellSouth and Certain Affiliated Companies, Dec. 17, 1993 ("Joint Audit").

[25] Id. at 11 (Attachment 3).

[26] See id. ("obstructionist behavior" began in "May of 1992" and continued through at least December 1993).

[27] Id.